[redacted]

Supreme Court of the United States

[redacted]

No. 1[redacted] 318

[redacted]

[redacted]

[redacted]

[redacted]

CONTENTS.

PAGE

Petition for Writ of Certiorari 1
Statement of the Issue 1
Statement of the Facts 2
Reasons for Review 6
Brief in Support of Petition 9
Statement of the Issue 9
Argument 10

FIRST POINT.

THE PETITIONER WAS NOT PUT ON NOTICE BY CHECKS DRAWN BY THE PLAINTIFF'S AGENT ON HIS PRINCIPAL'S FUNDS TO HIS OWN ORDER AND TENDERED FOR THE CREDIT OF HIS PRIVATE ACCOUNT 10

a. *The authorities relied upon by the Court below are, save in two instances, obiter dicta* ... 16

b. *The Court below is in direct conflict with the Court of Appeals of New York on the effect of certification* 18

SECOND POINT.

THE THEORY OF NOTICE APPLIED BY THE COURT BELOW IS CONTRARY TO THE DECISIONS OF THIS COURT 21

LAST POINT.

THE PETITION FOR A WRIT OF CERTIORARI SHOULD BE GRANTED 24

TABLE OF CASES CITED.

PAGE

Allen v. Puritan Trust Co., 211 Mass. 409, 423 . . 11, 13, 14
A. L. Underwood, Ltd. v. Bank of Liverpool, (1924) 1 K. B. 775 16
Anderson v. Kissam, 35 Fed. 699 17

Bank of Hickory v. McPherson, 102 Miss. 852 . . . . . 13, 16
Batchelder v. Central National Bank, 188 Mass. 25 . . 12
Bischoff v. Yorkville Bank, 218 N. Y. 106 . . . . . 12, 14
Brookhouse v. Union Publishing Co., 73 N. H. 368 12

Carnegie Trust Co. v. First Nat. Bank, 213 N. Y. 301 . 19
Charleston Paint Co. v. Exchange Banking Co., 123 S. W. Rep. (S. C.) 830 12
City of Newburyport v. First National Bank, 216 Mass. 304 12
City of Newburyport v. Spear, 204 Mass. 146, 150 11
Coleman v. Bucks & Oxen Union Bank, (1897) 2 Ch. 243 12
Commercial Savings Bank v. National Surety Co., 294 Fed. 261 11

Duckett v. Mechanics Bank, 86 Md. 400 12

Farmers' Loan & Trust Co. v. Fidelity Trust Co., 86 Fed. 541 17
Fidelity & Deposit Co. v. Queens County Trust Co., 226 N. Y. 225 11
Freund v. Imp. & T. Nat. Bank, 76 N. Y. 352 19

Gallo v. Brooklyn Savings Bank, 199 N. Y. 222 19
Gate City Building & Loan Assn. v. National Bank, 126 Mo. 82 . . . . . 12, 15
Goodwin v. American Nat. Bank, 48 Conn. 550 . . 12, 14, 15

PAGE

Goshen Nat. Bank v. State of N. Y., 141 N. Y. 379.. 19
Gray v. Johnston, L. R. 3 Eng. & Ir. App. 1.....12, 16

Hambro v. Burnand, (1904) 2 K. B. 10..... 10
Harvard Law Review, 454 (March, 1921)..... 15
Havana Central Railroad Co. v. Knickerbocker Trust Co., 198 N. Y. 422.....6, 10, 15
Havana Central Railroad Co. v. Central Trust Co., 204 Fed. 546.....10, 17
Hood v. Kensington Nat. Bank, 230 Penn. St. 508.....12
Hotchkiss v. National Banks, 21 Wall. 354, 359..... 22

Interstate National Bank v. Claxton, 97 Texas 569.. 12

Jueth v. National Bank of the Commonwealth, 56 N. Y. 478, 480..... 19

Kendall v. Fidelity Trust Co., 230 Mass. 238...11, 14, 15

Lloyd v. Grace, Smith & Co., (1912) A. C. 716..... 10

McCullam v. Third National Bank, 237 S. W. Rep. (Mo.) 1051..... 12
Mannerlyn v. Bank, 88 Ga. 333..... 12
Manufacturers Trust Co. v. United States Mortgage & Trust Co., 122 Misc. (N. Y.) 726..... 13
Martin v. Bank, 66 Kan. 655..... 12
Merchants Bank v. State Bank, 10 Wall. 604, 648.... 19
Meuer v. Phenix Nat. Bank, 94 App. Div. 331; 183 N. Y. 511..... 19
Mott Iron Works v. Metropolitan Bank, 78 Wash. 294.....12, 14-15

Murray v. Lardner, 2 Wall. 110, 121..... 22
National Bank v. Insurance Co., 104 U. S. 54..... 9
National Safe Deposit Co. v. Hibbs, 229 U. S. 391.... 24
Negotiable Instruments Law, Sec. 95 (N. Y.)..... 23
Norton v. City Bank & Trust Co., 294 Fed. 839, 845.. 23

PAGE

Oklahoma State Bank v. Galion Iron Works, etc., 4 Fed. (2nd) 337 17

Postal Telegraph Cable Co. v. Citizens Nat. Bank, 228 Fed. 601 (3rd Cir., C. C. A.) 23

Safe Deposit & Trust Co. v. Bank, 194 Pa. St. 334 ..12, 15
Sagone v. Mackey, 225 N. Y. 594, 599 14
Santa Marina Co. v. Canadian Bank, 254 Fed. 391 .6, 11, 15
Shields v. Bank of Ireland, (1901) 1 Irish Reports 222 12
Southern Trust & Commerce Bank v. San Diego Savings Bank, 212 Pac. Rep. (Calif.) 385 12
Squire v. Ordemann, 194 N. Y. 394 13
State v. Chicago Bonding Co., 215 S. W. Rep. (Mo.) 21 12
State v. Farmers & Merchants Bank, 201 N. W. Rep. (Neb.) 897 12
A. L. Underwood, Ltd. v. Bank of Liverpool, (1924) 1 K. B. 775 16

Union Stock Yards Bank v. Gillespie, 137 U. S. 411 .. 9
United States F. & G. Co. v. Home Bank, 77 W. Va. 665 12
United States F. & B. Co. v. First Nat. Bank, 18 Calif. App. 437 12
United States F. & G. Co. v. Peoples Bank, 127 Tenn. 720 .....13, 16

Warren-Scharf Asphalt Paving Co. v. Commercial National Bank, 97 Fed. 181, 185, 186 10
Whiting v. Hudson Trust Co., 234 N. Y. 394
6, 11, 13, 15, 16, 19
Wickenheiser v. Colonial Bank, 168 App. Div. 329; 225 N. Y. 650 14

Supreme Court of the United States

EMPIRE TRUST COMPANY, Petitioner-Defendant, against CHARLES HAZLITT CAHAN, Respondent-Plaintiff.	October Term, 1925. No.

Sirs:

PLEASE TAKE NOTICE that the annexed petition for a writ of *certiorari* will be presented to the Supreme Court of the United States on Monday, March , 1926.

Dated, New York, March , 1926.

VAN VECHTEN VEEDER,

WILLIAM LEE WOODWARD,

Counsel for Petitioner.

To:

HUGHES, ROUNDS, SCHURMAN & DWIGHT, Esqs.,
Counsel for Respondent.

Supreme Court of the United States

EMPIRE TRUST COMPANY, Petitioner-Defendant, against	October Term, 1925.
CHARLES HAZLITT CAHAN, Respondent-Plaintiff.	No.

PETITION FOR CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Your petitioner, the Empire Trust Company, a New York corporation, respectfully shows:

I.

Statement of the Issue.

FIRST: This is a petition for a writ of certiorari to review a decision of the United States Circuit Court of Appeals for the Second Circuit, which affirmed a judgment of the United States District Court for the Southern District of New York in favor of the plaintiff in an action at law.

SECOND: The plaintiff sued to recover the proceeds of twenty-one checks, aggregating $31,170, drawn by plaintiff's son, Charles H. Cahan, Jr., on funds of the plaintiff on deposit in the Guaranty Trust Company and with the Agents of the Bank of Montreal, both in the City of New York, under powers of attorney to said Cahan, Jr., executed by the plaintiff. The checks which (save in two instances) were certified by the banks on which they were drawn, were deposited by Cahan, Jr., to the credit of his personal account in the Empire Trust Company, the defendant, and the proceeds were thereafter drawn by him and used for purposes unknown to the plaintiff.

THIRD: The issue, as stated by the Court below, is:

> "Admittedly defendant knew nothing of what its depositor Cahan, Jr., was doing except as information was given by the cheques he offered for deposit; wherefore, the record presents this bald legal question: is an agent's bank of deposit put on notice by, and does it take at its peril if it receives without investigation, a check drawn by the agent on his principal's funds to his own order and tendered for the credit of his private account?" (Record, pp. 269-270).

II.

Statement of the Facts.

FOURTH: The plaintiff, a Canadian barrister, was employed during the war in supervising British munition contracts in this country. The magnitude of the work led him to establish his headquarters in New York City in January, 1915, and in May of that year, his son, Charles H. Cahan, Jr., also a Canadian barrister, joined him as an assistant. Father and son lived together, the former

paying the living expenses and direct compensation to the son.

FIFTH: The plaintiff's duties required much travel. He was frequently in England and traveled throughout the United States. In view of his frequent and long continued absence from New York, he gave his son in 1916, broad powers of attorney on personal accounts carried by him in two New York City banks, namely, the Agents of the Bank of Montreal and the Guaranty Trust Company (Record, fols. 466, 481).

SIXTH: The plaintiff's work no longer required residence here after the United States entered the war, and he and his son returned to Montreal in the summer of 1917. Meanwhile, Cahan, Jr., had opened an account of his own in the Empire Trust Company on September 29, 1915. The account is printed in full in the Record, pages 197 to 214. The aggregate deposits to August 4, 1919, when the account was closed, amounted to $70,742.08.

SEVENTH: In December, 1919, the discovery of irregularities in his accounts in Montreal and the disappearance of his son led the plaintiff to inquire about his deposits in the New York banks, to which he had paid no attention after giving his son authority over them (Record, fols. 283, 284). In January, 1920, the plaintiff discovered in his son's safe deposit box in Montreal twenty of the cancelled checks on the Guaranty Trust Company and the Agents of the Bank of Montreal upon which this suit was brought, showing collection thereof by the defendant bank, which apprised him for the first time of the existence of his son's personal account (Record, fols. 133-135).

The face, form and contents of the checks (save one which was not found) are printed in full on pages 163 to

183 of the record. All the checks are signed "C. H. Cahan, by C. H. Cahan, Jr., His Attorney." Seventeen of the twenty-one checks are payable to the order of Cahan, Jr., three to the order of the Empire Trust Company (Plaintiff's Exhibits 5-c, 5-d and 5-j, Record, fols. 496, 499, 517). All the checks, save two (Plaintiff's Exhibits 5-r and 5-s, fols. 541-544), were either certified by the Guaranty Trust Company or accepted by the agents of the Bank of Montreal, according to whether they were drawn on one or the other bank. Thus certified before presentation (Record, fols. 381-388, 394-397), all the checks were deposited by Cahan, Jr., to the credit of his account with the defendant bank. Each deposit was accompanied by a deposit slip (Record, fol. 394), save two (Defendant's Exhibits A-1 and A-2, Record, fols. 668-671) received by mail (Record, fols. 378-380, 652-654), for which deposit slips were made out by defendant's receiving teller.

EIGHTH: The defendant made no loans to Cahan, Jr. (Record, fols. 437, 438), nor did it receive any of the checks in payment of overdrafts. The plaintiff's attempt by cross-examination on the trial (Record, fols. 328-365, 393-420) and on argument in the Court below, to develop a theory of "threatened" overdraft, was ignored by the Court below and need not be discussed at this time.

NINTH: The plaintiff testified that the authority given to his son was intended by him to be exercised only in payment of his own personal expenses (Record, fol. 276). Whether this intention was ever communicated to his son does not appear; nor is it known, even now, what disposition the son made of the proceeds of the checks in issue (Record, fols. 146-148). The plaintiff testified (Record, fol. 146), as alleged in his complaint, that the proceeds had not been used for his purposes. The sole attempt to

prove actual misappropriation was by reference to his son's entries on the stubs of the check books of the depository banks (Record, fols. 147-148). But the plaintiff's admission of ignorance of the use made of the money is explicit: "I do not know what he did with it. I have no definite knowledge" (Record, fol. 271). Of course, the defendant had none of the cancelled checks which had been taken up by Cahan, Jr., nor any record of the payees (Record, fols. 370-371). It had only deposit slips which accompanied the checks in issue, which it produced (Record, fols. 203-207).

TENTH: Pursuant to stipulation, the case was tried by a jury of one, on motion of each party for a directed verdict (Record, fols. 86, 458, 459). The District Judge directed a verdict in favor of the plaintiff for $31,170, the aggregate amount of the checks in issue, without interest (Record, fols. 464, 722-732). Both parties assigned error, the defendant upon the direction of the verdict (Record, fols. 740-743) and the plaintiff on the disallowance of interest (Record, fols. 770-774).

ELEVENTH: The Circuit Court of Appeals affirmed the judgment of the District Court with respect to the principal amount, the face value of the twenty-one checks in issue; and, reversing the judgment below to this extent, allowed interest thereon from the dates when they were respectively credited by the defendant to Cahan, Jr. (Record, pp. 266-285). It held expressly that Cahan, Jr., had both actual and apparent authority to draw the checks, but that his misappropriation lay in what he did with them. Admitting that the defendant knew nothing of what its depositor, Cahan, Jr., was doing beyond the information given by the checks offered for deposit, the Court nevertheless held that an agent's bank of deposit

is put on notice by, and takes at its peril if it receives without investigation, a check drawn by the agent on his principal's funds to his own order and tendered for the credit of his private account.

III.

Reasons for Review.

TWELFTH: This case involves a question of commercial law applicable to all banks and individuals dealing with checks, drafts and notes negotiated by corporate officers, agents and other fiduciaries. Inasmuch as such persons transact, in their representative capacity, the greater part of modern business, it is important that the legal status of their commercial paper be certain and uniform.

The decision of the Circuit Court of Appeals *expressly* conflicts with the recent decision of the Court of Appeals of New York in *Whiting* v. *Hudson Trust Co.*, 234 N. Y. 394, and the earlier decision in *Havana Central Railroad Co.* v. *Knickerbocker Trust Co.*, 198 N. Y. 422, as well as with the decision of the Circuit Court of Appeals for the Ninth Circuit in *Santa Marina Co.* v. *Canadian Bank of Commerce*, 254 Fed. 391.

The decision of the Court below is, moreover, contrary to the law as declared by the Circuit Courts of Appeals for the Third and Sixth Circuits, by the courts of last resort in Massachusetts, Connecticut, Pennsylvania, Maryland, West Virginia, Missouri, California, Washington, and other States, and by the House of Lords.

In fact, only two actual decisions, in Tennessee and Mississippi, support the judgment below, and the former is by a divided Court. In the other cases cited by the Court below reliance is placed upon dicta, as distinguished from the issue decided.

THIRTEENTH: The decision of the Court below is based upon a theory of notice which is in direct conflict with repeated decisions of this Court.

WHEREFORE, your petitioner, referring to the attached brief in support of the foregoing reasons for review, respectfully prays that this Honorable Court issue a writ of certiorari directing the Circuit Court of Appeals for the Second Circuit to certify and send to this Court a full and complete transcript of the record herein, to the end that the said cause may be reviewed and determined by this Court, as provided by law; and that the judgment of the Circuit Court of Appeals herein may be reversed, and that your petitioner may have such other and further relief or remedy in the premises as to this Honorable Court may seem meet and just.

EMPIRE TRUST COMPANY,
By PAUL H. HUDSON,
Vice-President.

VAN VECHTEN VEEDER,
WILLIAM LEE WOODWARD,
Counsel for Petitioner.

STATE OF NEW YORK, }
COUNTY OF NEW YORK, } ss.:

PAUL H. HUDSON, being duly sworn, says:

I am Vice-President of the Empire Trust Company, a corporation organized under the laws of the State of New York, the petitioner herein, and I have knowledge of this litigation. The foregoing petition and the matters therein set forth are true, to the best of my knowledge, information and belief.

PAUL H. HUDSON.

Sworn to before me this
11th day of March, 1926

FRANK E. SCHWERTZ, Notary Public, Kings County
Kings County Clerk's No. 936, Register's No. 7512
Certificate filed New York County
Clerk's No. 1111, Register's No. 7800
Term expires March 30, 1927

WE HEREBY CERTIFY that we have examined the foregoing petition, that in our opinion it is well founded and entitled to the favorable consideration of the Court, and that it is not filed for the purpose of delay.

VAN VECHEN VEEDER,
WILLIAM LEE WOODWARD,
Counsel for Petitioner.

Supreme Court of the United States

EMPIRE TRUST COMPANY, Petitioner-Defendant, against CHARLES HAZLITT CAHAN, Respondent-Plaintiff.	October Term, 1925. No.

BRIEF IN SUPPORT OF PETITION.

Statement of the Issue.

One who deals with commercial paper drawn by a fiduciary (whether a mere agent or formal trustee) may become liable for the fiduciary's misappropriation of funds:

First, by a violation of the contract of deposit between the owner of the funds and his depositary bank; in other words, by payment without authority;

Second, by participating in a diversion of the funds with knowledge or notice of the fraud; for example, by appropriating the funds in payment of the fiduciary's indebtedness. *National Bank* v. *Insurance Co.*, 104 U. S. 54; *Union Stock Yards Bank* v. *Gillespie*, 137 U. S. 411.

The Court below held that the plaintiff's agent "had both actual and apparent authority to draw the twenty-one checks" (Record, p. 270). No other conclusion with

respect to the agent's authority would have been possible under the decisions. *Warren-Scharf Asphalt Paving Co.* v. *Commercial National Bank*, 97 Fed. 181, 185-186 (C. C. A., 6th Cir.); *Hambro* v. *Burnand*, (1904) 2 K. B. 10; *Lloyd* v. *Grace, Smith & Co.*, (1912) A. C. 716.

"Admittedly," said the Court below, "defendant knew nothing of what its depositor Cahan, Jr., was doing except as information was given by the cheques he offered for deposit; wherefore, the record presents this bald legal question: is an agent's bank of deposit put on notice by, and does it take at its peril if it receives without investigation, a check drawn by the agent on his principal's funds to his own order and tendered for the credit of his private account?" (Record, pp. 269-270). Following a dictum in its prior decision in *Havana Central Railroad Co.* v. *Central Trust Co.*, 204 Fed. 546, which it admits is nowhere else stated in such "compendious and far-reaching form" (Record, p. 278), and feeling "acutely the disadvantage of continuing to differ with the highest Court of New York" (Record, p. 282), the Court below decided the issue in favor of the plaintiff.

FIRST POINT.

The petitioner was not put on notice by checks drawn by the plaintiff's agent on his principal's funds to his own order and tendered for the credit of his private account.

In reaching its result the Court below ignored the fact that the form of the checks drawn to the agent's order imported ownership of the proceeds in Cahan, Jr. The possession of a bank check payable to the order of the holder is presumptive evidence of ownership. *Havana Central Railroad* v. *Knickerbocker Trust Co.*, 198 N. Y.

422, 428. Cahan, Jr., was the payee of these checks with power to collect them. The instruments were collected according to their tenor for the account of the very person therein named as payee. *Whiting* v. *Hudson Trust Co.*, 234 N. Y. 394, 403, 406, where Judge Cardozo distinguished such a case from those in which the depositor had no title to the paper (pp. 405-406). Judge Cardozo was dealing with the case of a corporate officer endorsing to himself checks received by the corporation and drawn to its order as payee, but several of the cases upon which the Court below relied belong in this category (see *infra*, p. 16).

However, whether subject to a trust or not, the deposit of the checks to the credit of Cahan, Jr., would not constitute notice of diversion or misappropriation. The plaintiff had entrusted authority over his funds to his son. The deposit with the defendant bank did not operate to take the funds out of his son's control. So long as the funds remained in Cahan, Jr.'s control they were not diverted. A fiduciary having general authority to draw checks must of necessity have authority to direct their disposition. His authority in this respect can of course be limited; but in the absence of limitations of which the person receiving the checks has knowledge on notice, it may be assumed that it is unlimited. Accordingly, it is almost universally held that a fiduciary, of whatever kind, may deposit the funds of his principal in a bank to his individual credit.

***Santa Marina Co.* v. *Canadian Bank*,** 254 Fed. 391 (certiorari denied 250 U. S. 643); *Commercial Savings Bank & Trust Co.* v. *National Surety Co.*, 294 Fed. 261. *Whiting* v. *Hudson Trust Co.*, 234 N. Y. 394; *Fidelity & Deposit Co.* v. *Queens County Trust Co.*, 226 N. Y. 225; *Kendall* v. *Fidelity Trust Co.*, 230 Mass. 238; *Allen* v. *Puritan Trust Co.*, 211 Mass. 409, 423; *City of Newburyport* v. *Spear*, 204 Mass. 146, 150; *Batchelder* v. *Central*

National Bank, 188 Mass. 25; *Goodwin* v. *American National Bank*, 48 Conn. 550; *Brookhouse* v. *Union Publishing Co.*, 73 N. H. 368; *Hood* v. *Kensington National Bank*, 230 Penn. St. 508; *Duckett* v. *Mechanics Bank*, 86 Md. 400; *United States Fidelity & Guaranty Co.* v. *Home Bank*, 77 W. Va. 665; *McCullam* v. *Third National Bank*, 237 S. W. Rep. (Mo.) 1051; *Gate City Building & Loan Assn.* v. *National Bank*, 126 Mo. 82; *Mott Iron Works* v. *Metropolitan Bank*, 78 Wash. 294; *Southern Trust & Commerce Bank* v. *San Diego Savings Bank*, 212 Pac. Rep. (Calif.) 385; *United States Fidelity & Banking Co.* v. *First National Bank*, 18 Calif. App. 437; *Interstate National Bank* v. *Claxton*, 97 Texas 569.

Gray v. *Johnston*, L. R. 3 Eng. & Ir. App. 1; *Coleman* v. *Bucks & Oxon Union Bank*, (1897) 2 Ch. 243; *Shields* v. *Bank of Ireland*, (1901) 1 Irish Reports 222.

If he possess the right to do so, it must necessarily follow that the bank has the right to accept the deposit. Knowledge on the part of the bank of the nature of the funds received does not affect the character of the act. The bank has the right to presume that a fiduciary will apply the funds to their proper use under the trust. *Bischoff* v. *Yorkville Bank*, 218 N. Y. 106; *City of Newburyport* v. *First National Bank*, 216 Mass. 304; *Safe Deposit & Trust Co.* v. *Bank*, 194 Penn. St. 334; *Mannerlyn* v. *Bank*, 88 Ga. 333; *Martin* v. *Bank*, 66 Kan. 655; *State* v. *Chicago Bonding Co.*, 215 S. W. Rep. (Mo.) 21; *State* v. *Farmers & Merchants Bank*, 201 N. W. Rep. (Neb.) 897; *Charleston Paint Co.* v. *Exchange Banking Co.*, 123 S. W. Rep. (S. C.) 830; and cases cited *supra*.

This is the settled law of New York. The Court of Appeals said in *Bischoff* v. *Yorkville Bank*, 218 N. Y. 106, 111:

> "A fiduciary may legally deposit the trust funds in a bank to his individual account and credit.

> Knowledge on the part of the bank of the nature of the funds received and credited does not affect the character of the act. The bank has the right to presume that the fiduciary will apply the funds to their proper uses under the trust. There are judicial decisions, in cases in which the fiduciary has converted the funds, which hold the contrary (*U. S. Fidelity & G. Co.* v. *Peoples Bank*, 127 Tenn. 720; *Bank of Hickory* v. *McPherson*, 102 Miss. 852). The rule stated by us is, however, established in this and other jurisdictions, as the decisions hereinafter cited will disclose, and accords with reason."

In the recent case of *Whiting* v. *Hudson Trust Co.*, 234 N. Y. 394, at pages 402-403, Judge Cardozo said:

> "What it did was to accept the check for the use of the depositor upon an agreement that the proceeds should be subject to his order. When the order was given and the money disbursed, the situation was the same as if cash had been delivered for safekeeping and afterwards returned. In such a situation, the defendant is to be held liable, if at all, only upon a showing that by the form of the account it has facilitated a conversion and made itself, in so doing, a party to a tort (*Allen* v. *Puritan Trust Co.*, 211 Mass. 409, 422; *Squire* v. *Ordemann*, 194 N. Y. 394). But nothing that was done by the defendant did facilitate a conversion. Eckerson was the payee of the check with power to collect it. His power was neither increased nor diminished by the form of the deposit. He was the owner of a chose in action whether subject to a trust or free from one. Under the law as it then stood,* a trus-

---

* This refers to the provisions of Chapter 588 of the Laws of 1916 (now Sections 104 and 231 of the Surrogates' Court Act), whereby an executor, administrator, guardian or other testamentary trustee is required to invest or deposit funds as such, on pain of removal and of misdemeanor. This statute does not change the rule of law relating to the liability of a bank receiving checks for deposit by the testamentary trustee in his own name (*Manufacturers' Trust Co.* v. *United States Mortgage & Trust Co.*, 122 Misc. 726, 730-732).

> tee did not convert the moneys of the trust by the mere act of depositing them in a bank in his individual name (*Bischoff* v. *Yorkville Bank, supra; Sagone* v. *Mackey*, 225 N. Y. 594, 599; *Wickenheiser* v. *Colonial Bank*, 168 App. Div. 329, 333; 224 N. Y. 650)."

Such is the uniform rule in Massachusetts. In *Kendall* v. *Fidelity Trust Co.*, 230 Mass. 238, where the facts are precisely in point, the Court said:

> "As the defendant had no interest in the deposits and never received any part thereof for the payment of any debt due it, but credited all amounts so collected to Alvero's personal account, it cannot be charged with constructive notice of the fraudulent conduct of the fiduciary. * * * The weight of authority is in accord with the view that if a bank, acting in good faith, merely credits trust funds, knowing them to be such, to the personal account of the fiduciary, it will not be liable if he later misappropriates such funds. Cases cited in Note to Allen v. Puritan Trust Co., L. R. A. 1915, C. 518. As the defendant cannot be charged with constructive notice of the fraudulent acts of Alvero merely because of the form of the checks and because the amounts collected thereon were deposited in his personal account with other funds deposited by him, it follows that there is no evidence that the defendant knew he intended to misappropriate the funds and the defendant therefore cannot be held liable."

See also *Goodwin* v. *American National Bank*, 48 Conn. 350, and *Mott Iron Works* v. *Metropolitan Bank*, 78 Wash. 294.

The plaintiff seeks to distinguish the case of *Bischoff* v. *Yorkville Bank*, 218 N. Y. 106, *supra*, on the ground that the acts of an executor were there involved, and that the Court pointed out that an executor has title to the

assets in his hands. We quote the Court's statement of the legal principle applicable to fiduciaries, which the cases cited by the Court show does not depend upon any consideration of legal title. The rule has been applied in numerous cases in which the fiduciary had no legal title: agents, attorneys, corporate officers, public officers, etc. *Kendall* v. *Fidelity Trust Co.*, 230 Mass. 238; *Safe Deposit & Trust Co.* v. *Bank*, 194 Pa. St. 334; *Whiting* v. *Hudson Trust Co.*, 234 N. Y. 394; *Mott Iron Works* v. *Metropolitan Bank*, 78 Wash. 294; *Santa Marina Co.* v. *Canadian Bank*, 254 Fed. 391; *Havana Central Railroad Co.* v. *Knickerbocker Trust Co.*, 198 N. Y. 422; *Gate City Building & Loan Assn.* v. *National Bank of Commerce*, 126 Mo. 82; *Goodwin* v. *American National Bank*, 48 Conn. 550.

On principle there can be no valid distinction since possession of a check payable to the order of the holder is presumptive evidence of ownership. *Havana Central R. R. Co.* v. *Knickerbocker Trust Co.*, 198 N. Y. 422, 428; *Whiting* v. *Hudson Trust Co.*, 234 N. Y. 394, 402, 403. This subject is covered fully in an article by Professor Scott in 34 Harvard Law Review, 454 (March, 1921). He treats trustees and agents as being in the same category. At pages 469-470 he cites numerous decisions and states the law as follows:

> "Thus, if a trustee or other fiduciary indorses a check payable to him as trustee and deposits the same to the credit of his individual account, the bank is under no duty to make inquiry as to the propriety of the depositor's conduct. So too if a trustee draws a check upon an account in another bank standing in his name as trustee, and deposits the same to his individual credit with the defendant bank, the latter bank is not bound to inquire as to the propriety of the trustee's conduct."

There is no liability for participation in the wrongdoing of a fiduciary unless the person dealing with him acts in bad faith or is in some way chargeable with notice of his misconduct. Since this is the test of liability, it is immaterial whether the fiduciary is a trustee with legal title or an agent with a power of disposition.

(a) *The authorities relied upon by the Court below are, save in two instances, obiter dicta.*

The meagreness of authority to the contrary is apparent from the opinion of the Court below.

The Court below is clearly in error in supposing that the Court of Appeals avoided the issue in *Whiting* v. *Hudson Trust Co.*, 234 N. Y. 394, by relying upon certification. The issue was squarely decided without regard to certification, which was dealt with as a separate and additional consideration.

Among the other State court cases relied upon by the Court below, only two actually decided the issue herein: *U. S. Fidelity & Guaranty Co.* v. *People's Bank*, 127 Tenn. 720, and *Bank* v. *Hickory* v. *McPherson*, 102 Miss. 852; and the former is by a divided court.

The plain difference between the recent English case of *A. L. Underwood, Ltd.* v. *Bank of Liverpool*, (1924) 1 K. B. 775, is that, as the court held, Underwood did not purport to act in the transaction under any authority from the corporation. The checks on their face imported ownership in the company, not in him. The purport of his dealing with them as he did was, not that he acted as agent for the company, but that he acted for himself as principal. As viewed by the Court below, the judgment of the Court of Appeal would be in conflict with the decision of the House of Lords in *Gray* v. *Johnston*, L. R. 3 Eng. & Ir. App. 1. In the latter case the bank was absolved even though the deposits were applied, in ordinary

business routine, to an overdrawn account; "it appears to me wholly impossible to imagine," said Lord Cairns, "that the bankers can have been influenced in any degree in their conduct by the indirect and incidental benefit which they thus derived."

The Court below relied upon *dicta* in two of its prior decisions, *Havana Central R. R. Co.* v. *Central Trust Co.*, 204 Fed. 546, and *Anderson* v. *Kissam*, 35 Fed. 699. Since the former was a suit against the drawee bank, any expression of opinion concerning the liability of the agent's depository bank was necessarily *obiter;* the actual decision was that where a corporate check is drawn by an officer, with express or implied authority to draw it, a bank is not put upon inquiry by the fact that it is drawn to his own order and may be improperly used. *Anderson* v. *Kissam* is not in point, since it was a case of actual notice of fraud. The defendants, who were stock-brokers, applied the proceeds of checks drawn by a bank cashier to the latter's account for margins in stock speculation.

The majority opinion of the Circuit Court of Appeals for the Ninth Circuit in *Farmers' Loan & Trust Co.* v. *Fidelity Trust Co.*, 86 Fed. 541, is based expressly upon the fact that the agent asked for and received from the bank a certificate of deposit in his individual name, which was held to be equivalent to a declaration by him that the money was received by him for his individual use. The dissenting opinion denied that the circumstance that a certificate of deposit was obtained was of itself calculated to put the bank upon inquiry as to the use to which the money was to be put.

The Court below relies upon a statement of law made by the Circuit Court of Appeals for the Eighth Circuit in *Oklahoma State Bank* v. *Galion Iron Works & Mfg. Co.*, 4 Fed. (2d) 337. This statement of law is not sustained

by any one of the cases cited in its support, all of which are either cases of clear lack of authority or of actual notice of fraud. The case was decided on lack of authority. A manufacturing company which sold its machinery to township boards and county commissioners through sales agents, received payment, after appraisal, by means of warrants on township and county treasurers. Sales agents receiving these warrants were required to transmit them to the home office of the company, which collected them when funds were available in the respective treasuries to pay them. A sales agent endorsed a number of these warrants in the name of the company, discounted them with the defendant bank, placed the proceeds to his individual credit, and afterward drew out and appropriated the proceeds. The bank was of course held liable. Obviously, the agent had no authority to endorse the warrants. And the face of the warrants imported ownership in the principal, not in the agent. The ground upon which the decision proceeds is, when a bank with knowledge that its funds belong to the principal and not the agent, which was apparent on the face of the warrants, permits him to deposit funds collected by him for his principal with a bank to his own individual credit, and draw them for his own personal and private use, it is liable to the principal for the moneys, "unless the agent acted within the apparent scope of his authority, which is not claimed."

(b) *The Court below is in direct conflict with the Court of Appeals of New York on the effect of certification.*

The Court below also took direct issue with the Court of Appeals of New York on the effect of certification. In

Whiting v. *Hudson Trust Co.*, 234 N. Y. 394, 404, Judge Cardozo said:

> "The payee of the check, before delivering it to the defendant, had caused it to be certified. The legal result was the same as if he had received the cash over the counter (*Freund* v. *Imp. & T. Nat. Bank*, 76 N. Y. 352; *Carnegie Trust Co.* v. *First N. Bank of N. Y.*, 213 N. Y. 301; *Meuer* v. *Phenix Nat. Bank*, 94 App. Div. 331; 183 N. Y. 511). Between the drawee bank and its depositor, the check had been paid (Neg. Inst. Law, §324; Consol. Laws, ch. 38; *Gallo* v. *Brooklyn Savings Bank*, 199 N. Y. 222). The payee was the owner of a chose in action, the drawee's promise to pay, just as much as if he were the holder of a cashier's draft (*Goshen Nat. Bank* v. *State of N. Y.*, 141 N. Y. 379; *Justh* v. *Nat. Bank of the Commonwealth*, 56 N. Y. 478, 480). What the defendant turned into money was not the obligation of the maker, but that of the drawee. In such circumstances, the act of collection for the account of the depositor was neither a conversion nor anything that had a proximate relation in aiding a conversion. The drawee would have paid in discharge of its own promise if Eckerson rather than the defendant had come to it with the check and demanded payment of the money. If this had been done, and the money then handed to the defendant, there would hardly be a claim that a tort would have resulted, though the money was received with knowledge of its origin. The intervention of a cashier's draft or its equivalent changes the transaction in form, but not in substance (*Goshen Nat. Bank* v. *State of N. Y.*, *supra*)."

In other words, as this Court said in *Merchants Bank* v. *State Bank*, 10 Wall. 604, 648:

> "The object of certifying a check, as regards both parties, is to enable the holder to use it as money. The transferee takes it with the same readiness and sense of security that he would take the notes of the bank. It is available also to him for all the purposes of money."

But the Court below disapproved of this view, saying:

> "We regard the certification of the cheques on Cahan, Sr.'s accounts as not controlling and are unable to agree with the reasoning of the Whiting case for the following reason. Let it be admitted as true (p. 404) that 'the legal result (of certification) is the same as if (Cahan, Jr.) had received the cash over the counter and * * * between the drawee-bank and its depositor (the present plaintiff) the cheques had been paid'; it remains true that this action, or any similar one, would have lain just as well if Cahan, Jr., had actually drawn the cash and deposited the same with defendant but had then cotemporaneously informed defendant that he had drawn the money from his father's account by virtue of his letter of attorney and now wished it to go to his personal credit and be available for his personal use" (Record, p. 275).

No authority was cited for this proposition, which is, in effect, that no bank can safely receive for deposit money said by an agent to have been drawn from his principal's funds. In other words, whenever a corporate officer or any other employee deposits checks or cash traceable to his principal, the legal presumption would be that the person making the deposit was a criminal and the bank would be required to make inquiry to establish the depositor's innocence. Such a rule would seriously clog the transaction of business, and would in effect make the banks insurers of the integrity of agents and other fiduciaries instead of placing the burden upon him whose misplaced confidence has made the wrong possible.

SECOND POINT.

The theory of notice applied by the Court below is contrary to the decisions of this Court.

The conclusion reached by the Court below was based upon an erroneous theory of notice. "The question in this case," the Court below said, is "whether there was sufficient notice in and by the face, form and contents of the cheque tendered for deposit" (Record, p. 278). And in deciding this question in the affirmative the Court took this view of notice:

> "It is never doubted that if a bank of deposit has notice which would lead that fiction of the law a 'reasonable man' to suspect wrong, the bank which fails either to verify or dispel that suspicion is responsible for the results" (Record, p. 278).

> "At bottom the question here depends upon whether the form of such drafts as those at bar gives clear enough notice that the agent is not acting in the principal's interest. There are indeed cases in which it might be in the principal's interest for the agent to withdraw funds from the principal's account and deposit them in his own account, even in a bank of the same city or in the same bank. The only case we can think of is one in which the agent wanted to conceal his principal's name in a transaction in which even a cashier's cheque might excite suspicion. But the payment of the agent's own debt might in fact be a part of such transaction, and that possibility does not seem to us sufficient justification. We must balance probabilities and conclude that we hold the form of the cheque should be taken as evidence that the agent is engaged upon ventures of his own, and as to his authority to conduct the same, the bank must assume the risk of investigation" (Record, pp. 281, 282).

While admitting that "it is a hard rule as business is ordinarily conducted" (Record, p. 282), "upon the whole we still incline" to "* * * yield that measure of assistance which the law increasingly attempts to give to the victims of misplaced confidence" (Record, p. 284).

This is in direct conflict with the settled rule in this Court in favor of holders for value before maturity that actual knowledge or wilful abstention from inquiry, where inquiry would have disclosed the infirmity is essential, and that mere negligence, or failure to inquire, where a reasonably prudent man would have inquired, will not suffice.

Thus in *Murray* v. *Lardner*, 2 Wall. 110, 121, this Court held:

> "Suspicion of defect of title or knowledge of circumstances which would excite such suspicion in the mind of a prudent man, or gross negligence on the part of the taker, at the time of the transfer, will not defeat his title. That result can be produced only by bad faith on his part.
>
> The burden of proof lies on the person who assails the right claimed by the party in possession."

This doctrine was reaffirmed in *Hotchkiss* v. *National Banks*, 21 Wall. 354, 359, where Mr. Justice Field said:

> "A suspicion that there is a defect of title in the holder, or a knowledge of circumstances that might excite such suspicion in the mind of a cautious person, or even gross negligence at the time, will not defeat the title of the purchaser. That result can be produced only by bad faith, which implies guilty knowledge or wilful ignorance, and the burden of proof lies on the assailant of the title."

This is now the statutory rule of notice in New York. New York Negotiable Instruments Law, Section 95 (same as Sec. 56 of the Uniform Negotiable Instruments Law):

> "To constitute notice of an infirmity in the instrument or defect in the title of the person negotiating the same, the person to whom it is negotiated must have had actual knowledge of the infirmity or defect, or knowledge of such facts that his action in taking the instrument amounted to bad faith."

And this provision was properly applied, contrary to the view of the Court below, in *Postal Telegraph-Cable Co. v. Citizens National Bank*, 228 Fed. 601 (3rd Cir., C. C. A.).

The result of the decision of the Court below is that the burden is cast upon the wrong party, reversing the equities of the situation. The equities are well described by the Circuit Court of Appeals for the Fourth Circuit in the recent case of *Norton v. City Bank & Trust Co.*, 294 Fed. 839, 845:

> "The accepted rule is neither arbitrary nor fanciful, but is both just and equitable. The owner of the fund trusts its agent. It tells the bank to pay out its funds on his order. As between him and the bank, the latter is bound to pay whomsoever he will. If any particular check is paid to a person whom he intended to receive it, the bank has done precisely what it was instructed to do. In such cases as that here involved, it is true that the agent has proved false to his trust, and some innocent person must be the loser. Should it not be the one who gave him the power which he misused?"

It is quite beside the point, therefore, to argue, as the Court below does, in support of its conclusion, that if